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S E C R E T SECTION 01 OF 05 KUALA LUMPUR 001259

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SUBJECT: SCENESETTER FOR THE VISIT OF CNO ADMIRAL MULLEN

Classified By: DCM David Shear for reasons 1.4 b and d.

11. (S) SUMMARY: Malaysian-American relations are good and improving; we are currently conducting negotiations for a Free Trade Agreement with Malaysia. This moderate, Muslim-majority state is our tenth-largest trading partner worldwide. Our robust and growing military-military cooperation is receiving greater public attention, along with some criticism from retrograde quarters. While moving slowly away from the anti-Western rhetoric of former Prime Minister Mahathir Mohamad, Malaysia continues to oppose us on some key international issues. Counterterrorism cooperation is largely good, but we remain concerned about the release of certain suspects and the level of surveillance of those suspects. Malaysia and its neighbors increasingly realize the importance of maritime security, but enforcement efforts are hampered by sovereignty concerns and a lack of resources. A new Malaysian coast guard is slowly getting its sea legs. Malaysia supports the Mindanao peace talks but has differed sharply with Thailand over separatist violence. The Malaysian government is making progress in implementing a non-proliferation regime, and we continue to press hard for endorsement of the Proliferation Security Initiative (PSI). End Summary.

Political Landscape

12. (C) While Malaysia has plenty of warts, it remains a rare example of an Islamic-majority country that is stable, civilian-led and prosperous. Malaysia has also maintained a largely tolerant social system and a tightly managed democracy, with the same multi-racial coalition in power since independence in 1957. While we continue to urge the government of Malaysia to improve its own governance, we also recognize the constructive role Malaysia can play in the Islamic world.

13. (C) Prime Minister Abdullah Badawi is a breath of fresh air after the long-serving and vituperative Mahathir Mohamad, who retired in late 2003. Abdullah promotes a tolerant, progressive approach to religion that he calls "Islam Hadhari" (civilizational Islam). He is publicly committed to fighting corruption and reining in costly mega-projects, though his government's follow-through has been disappointing. Corruption in government procurement, including defense contracts, remains a problem. Abdullah's mild-mannered and cautious approach has also led critics to question his leadership and effectiveness, but his ruling coalition remains secure. Abdullah's chief potential rival, Deputy Prime Minister (and Defense Minister) Najib Razak,

plays the role of a loyal bulwark. After two years in power, Abdullah has appealed to the public for patience in delivering reform. As long as the economy continues to grow healthily, the public will grant him that. Recent bitter criticism of Abdullah by Mahathir does reflect some nostalgia within the ruling party for more lavish spending and more decisive leadership, but does not directly threaten Abdullah, s hold on power.

¶4. (C) One of many subjects on which Mahathir has criticized Abdullah is the growing mil-mil cooperation between the United States and Malaysia, particularly with regard to the greater frequency of high-visibility ship visits. We have been pleased by the overwhelmingly positive media coverage our ship visits have received, in contrast to the quiet arrivals of past years. The flip side to this is that our visits are getting increased attention from ideological foes on the Islamic right, and from Mahathir, s opportunistic criticism. Deputy Prime Minister Najib has stoutly defended our cooperation before Parliament, and we do not see that our engagement is under threat. However, we do need to be cognizant of our increased military visibility and sensitive to GOM concerns, particularly with rising tensions in the Middle East, where Malaysians strongly sympathize with the Palestinians.

Economic Situation

¶5. (C) In his early days, PM Abdullah made rural development and control of government spending, partly as a means to encourage private sector led growth, his top economic priorities. So far, only his reduction of the government's deficit -- now down to 3.8 percent of GDP -- can be chalked

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up as a clear success. Abdullah's partisans say that the Ninth Malaysia Plan (9MP; a five year plan for economic policy and development spending) will be the vehicle for advancing his other economic goals, but the 9MP, unveiled on March 31, seemed more like "business as usual." 35% of the funding in 9MP is earmarked for completing projects started in 8MP. Abdullah has emphasized the need for fast implementation of 9MP (a tacit acknowledgment of the perceptions weak follow through by his government) and created a new government agency to focus on the problem.

¶6. (C) Meanwhile cuts in government subsidies for gasoline and diesel fuel -- one of the tools used to rein in the deficit -- have proved highly unpopular, and raised concerns about inflation. Increases in prices of other government-managed commodities, such as electricity, are in the works. For now, the economy is in reasonably good shape, with projected growth of around 5.0 percent in 2005 and official inflation of around 4.8 percent (although private analysts believe the real rate of price increases is much higher). However, the government may be facing a tough choice in the coming year between stimulating the economy to get back on a higher growth track, or raising interest rates to control inflation.

Malaysia's International Posture

¶7. (C) Malaysia currently is the chair of the Non-Aligned Movement (NAM), the Organization of the Islamic Conference (OIC) and of ASEAN. Malaysia hosted the ASEAN Summit and the East Asia Summit last December, and will host the ASEAN Regional Forum (ARF) ministerial this summer. Secretary of State Rice is plans to attend the ARF meetings in July. Malaysia backed the six-party DPRK nuclear talks and has supported Iraqi reconstruction efforts, but has been overeager to embrace Hamas and defend the Iranian nuclear program. The foreign ministry seems to be moving slowly away from some of Mahathir's anti-Western rhetoric and policies, but retains friendships with troublesome states like Cuba,

Zimbabwe, Sudan, Syria and Uzbekistan.

¶8. (C) The Malaysian government publicly supports China's "peaceful rise" and signed a defense cooperation MOU with China, despite lingering suspicions among senior Malaysian military officials of China's long-term intentions. An April visit by China's defense minister received very little coverage in the local press. While Malaysia and Singapore quarrel frequently over issues like water pricing, land reclamation, and transportation links, the two retain a loose defense relationship under the aegis of the Five Power Defense Arrangement (FPDA), along with the United Kingdom, Australia and New Zealand. Malaysia has actively supported peace efforts in the southern Philippines and Aceh in Indonesia. While a maritime boundary dispute with Indonesia in the Sulawesi Sea remains unresolved, Malaysia maintains generally good relations with all its ASEAN neighbors. Malaysia also enjoys good relations with India, and held their first navy-to-navy staff talks with India earlier this year. Deputy Prime Minister Najib visited India in June in a visit that many read as a careful attempt to build bridges with a long-term counterweight to China.

Counterterrorism

¶9. (S) Malaysia has generally been a reliable and constructive partner on counterterrorism. In 2003, Malaysia established the Southeast Asia Regional Center for Counterterrorism (SEARCCT), which now runs a full schedule of multilateral training courses, many conducted with U.S. support. Early round-ups in 2001 and 2002 of scores of Jemaah Islamiyah (JI) suspects crippled that organization's activities in Malaysia. Over 70 suspected terrorists remain in custody under the Internal Security Act (ISA), a "preventive" measure that has also been used to jail political opponents of the government in the past. To our knowledge, prosecutions and trials of the terrorist suspects are not planned. Drawing on their experience in defeating a communist insurgency, the Malaysians take a "rehabilitative" approach for some terrorists, keeping them under police supervision in "restricted residence." Several leading figures (such as JI financier Wan Min) have been released from ISA detention without warning. We remain concerned that surveillance of released terrorist suspects may be inadequate

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and their "rehabilitation" may be incomplete or insincere. JI, while weakened, still has the capability to strike here, and the Malaysians need to remain vigilant.

¶10. (C) While the Malaysian leadership firmly opposes terrorist organizations at home, it is deeply uncomfortable with any association of Islam with terrorism, and frequently lectures us on the need to eschew terms such as "Islamic terrorists" or "jihadists." Reflecting the broad support for the Palestinian cause among the majority here, the Malaysian government has no relations with Israel and often argues for the need to address the "root causes" of terrorism in the Middle East. In February, negotiators from the United States succeeded in reaching an agreement here on a text for a bilateral Mutual Legal Assistance Treaty (MLAT). We are hoping the treaty will be ready for signature in time for the Secretary of State's July visit. The treaty will be a good

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tool in fighting terrorism and other forms of transnational crime.

Maritime Security

¶11. (C) In July 2005, the insurer Lloyd's of London designated the Strait of Malacca (SOM) as a "war-risk zone," raising premiums for shippers transiting these waters. This prompted a flurry of public cooperation among the littoral

states -- Malaysia, Singapore and Indonesia, plus neighboring Thailand -- including conferences of foreign ministers and military chiefs. On September 13, 2005, the three littoral countries launched an "Eyes in the Sky" (EiS) program to conduct international aerial surveillance of the Strait. EiS originally comprised separate but coordinated flights by Malaysia and Singapore with observers from each of the three countries onboard each flight. Resource-strapped Indonesia did not contribute flights until the three countries signed an Agreement on 21 April 2006 that firmly set terms of reference and standard operating procedures. This Agreement states that "hot pursuit", which is a sensitive issue with the neighboring littorals, must be guided by bilateral agreements. Malaysia does not have a working bilateral hot pursuit agreement with either Singapore or Indonesia. Crews use binoculars to survey shipping traffic and make non-secure radio transmissions to shore and ship facilities of the three littoral states. Malaysia has also committed a single Beechcraft B-200 with infrared capability, to enable some night-time surveillance. Thailand continues to participate in discussions but the government has not given the military approval to join EiS.

¶12. (C) EiS represents an important symbolic step forward for the littoral states' cooperation on SOM security, but could be difficult to sustain without international support. DPM Najib has told the media on several occasions that Malaysia would welcome international involvement in Eyes in the Sky. Our working-level contacts remain vague, however, on what sort of American assistance might be accepted in this sovereignty-conscious region. Malaysia will host a meeting this September sponsored by the International Maritime Organization (IMO) in which the littoral states are to identify and prioritize their needs for assistance in enhancing SOM security. On February 15-17, the USG hosted a meeting of key SOM user states at Coast Guard Island, Alameda, California, to discuss the possible range and scope of such assistance.

¶13. (C) Meanwhile, the Sulu Sea remains an under-monitored passageway for terrorist elements in transit between Indonesia and Mindanao. Terror groups have also carried out a number of kidnappings for ransom in the area. While the region has little value for international shipping compared to the Malacca Strait, it is tremendously important to the travel and fundraising operations of groups like JI and Abu Sayyaf. Together with Embassies Jakarta and Manila, we have focused on this region as a specific theater for building capacity and cooperation between the governments of Malaysia, Indonesia and the Philippines. Significant new resources, which we are in the process of identifying and prioritizing, will be required to make these efforts successful.

New Coast Guard

¶14. (C) Malaysia's new coast guard began limited operations on November 30, 2005. The government's goal is to reduce

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overlap and turf battles among the 11 Malaysian agencies tasked with patrolling the country's seas and waterways. The coast guard, officially named the Malaysian Maritime Enforcement Agency (MMEA), will possess 72 vessels transferred from the navy, marine police, marine department, and fisheries department. MMEA has recruited about 1,300 personnel from these agencies, although the vast majority came from the Royal Malaysian Navy (RMN). The impact of the large, mid-grade officer exodus from the RMN to MMEA, in fact, has caused the RMN to halt any further transfers. RMN vessels transfer with their crews intact. MMEA hopes to fill its 4,000 approved positions within a year.

Mindanao Peace Talks, JI Presence

¶15. (S) Malaysia has facilitated peace talks between the Philippine government and the Moro Islamic Liberation Front (MILF), and the negotiations have had some success with the sticky issue of "ancestral domain." The talks are hosted by the Malaysian External Intelligence Organization, which in the past covertly supported separatist activities in Mindanao. JI presence at MILF training camps remains a concern, though the MILF has publicly disavowed any connection to JI. We continue to press the Malaysians to make clear to the MILF that it must sever its connections to JI and Abu Sayyaf.

Southern Thailand Strains Relations

¶16. (C) Separatist violence in southern Thailand has killed over 1,000 people since January 2004, and attacks continue almost daily. The Malaysian government has repeatedly denied Thai accusations that it supports the separatist groups, though the people on both sides of the porous border share Malay ethnicity and the Muslim religion. Families and business interests straddle the border as well. In August 2005 Malaysia offered temporary refuge to 131 Thai citizens who said they were fleeing their government's crackdown in the south. The issue, which has also involved the UN refugee agency, rubbed raw nerves in Kuala Lumpur and Bangkok, as government officials abandoned the usual neighborly ASEAN rhetoric for sharp verbal attacks on each other. The rhetoric toned down somewhat after the Malaysians returned one of the 131 asylum seekers, who was wanted on criminal charges in Thailand, but picked up again in June when the Thai Interior Minister claimed explosive devices set off in Thailand had been manufactured in Malaysia. The Thai MFA quietly retracted the charge, and the rhetorical cycle was reset to a cooling phase.

Slow Progress on Non-proliferation and PSI ...

¶17. (S) In 2003, a private Malaysian company (partly owned by PM Abdullah's son) was found to have manufactured and shipped nuclear centrifuge parts to Libya. The company pleaded ignorance, but the case underscored the need for Malaysia to adopt effective export controls. The government is moving ahead with plans to adopt such controls, including the conclusion of an Additional Protocol (AP) with the International Atomic Energy Agency (IAEA) on November 22, ¶2005. The AP provides a sound policy framework for the implementation of nuclear-related export controls.

¶18. (C) We continue to urge Malaysia to participate in Proliferation Security Initiative (PSI) meetings and exercises. Malaysia sent two observers in August 2005 to a PSI exercise in Singapore, and three observers in April 2006 to a PSI exercise in Australia. The government has said it supports PSI "in principle," and that it would take part in PSI operations on a case-by-case basis. We have been told that the government is considering an endorsement of the PSI Statement of Interdiction Principles, which would allow full participation in PSI events. However, elements within the foreign ministry remain adamantly opposed, perceiving that the PSI is targeted against "friends" of Malaysia, like Iran, Pakistan and China.

¶19. (S) As the chair of the Non-Aligned Movement (NAM), Malaysia has been too supportive of Iranian claims that its nuclear program is a peaceful one. More recently, the GOM has moved somewhat away from behavior that bordered on "coaching" the Iranians. The EU-3 made considerable efforts

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to get Malaysia to exert a restraining influence on Iran. While it appears the Malaysians have privately counseled Iran to exercise restraint, it does not seem these words had much influence on the Iranians. Malaysia failed to condemn Ahmadinejad's threat to "wipe Israel off the map" and gave

President Ahmedinejad a red carpet welcome in Kuala Lumpur as the IAEA was referring his repeated violations to the United Nations Security Council.
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